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No. 87-932

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

J.C. BRADFORD & CO.,
Petitioner,

vs.

SUZANNE KIRKPATRICK, DOROTHY D. CASLER
and CHARLES H. LINDSEY,
on behalf of themselves
and all other similarly situated,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

RESPONDENTS' BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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COUNTERSTATEMENT OF THE QUESTIONS PRESENTED FOR REVIEW

1. Is it appropriate for this Court to exercise its certiorari jurisdiction to review a decision of the United States Court of Appeals for the Eleventh Circuit which neither granted nor denied a motion for class certification in an action arising under the federal securities laws but, rather, remanded the matter to the District Court for further proceedings consistent with its decision?

2. Did not the Court of Appeals for the Eleventh Circuit properly conclude that the District Court, in ruling on a motion for class certification, was not permitted to disregard the allegations of respondents' Complaint and recharacterize the case in a manner which respondents neither pleaded nor intend to prove?

3. Did not the Court of Appeals for the Eleventh Circuit properly conclude that respondents were entitled to a presumption of reliance under the "fraud on the market" theory adopted by an *en banc* panel of the predecessor to that Circuit in *Shores v. Sklar*, 647 F.2d 462 (5th Cir. 1981) (*en banc*), *cert. denied*, 459 U.S. 1102 (1983)?

PARTIES TO THE PROCEEDING

The names of the parties to the proceeding are contained in the caption.

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RESPONDENTS' BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

Respondents Suzanne Kirkpatrick, Dorothy D. Casler and Charles H. Lindsey, on behalf of themselves and all other similarly situated ("respondents"), respectfully request that the Court deny the Petition for a Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit (the "Petition") submitted by J.C. Bradford & Co. ("petitioner") to review a judgment of the United States Court of Appeals for the Eleventh Circuit which reversed in part, affirmed in part and remanded an order of the United States District Court for the Northern District of Georgia denying respondents' motion for class certification.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Eleventh Circuit (App. Exhibit A)[1] is reported as *Kirkpatrick v. J. C. Bradford & Co.*, 827 F.2d 718 (11th Cir. 1987). The order of the Court of Appeals denying petitioner's petition for rehearing and suggestion of rehearing *en banc* is not reported and is set forth in the Appendix as Exhibit B. The order staying the mandate of the Court of Appeals is not reported and is set forth in the Appendix as Exhibit C.

The opinion of the United States District Court for the Northern District of Georgia denying respondents' motion for class certification (App. Exhibit D) is reported as *Sanders v. Robinson Humphrey/American Express, Inc.*, 634 F.Supp. 1048 (N.D. Ga. 1986). The District Court's opinion denying respondents' motion for reconsideration, granting respondents' motion to certify the case for interlocutory appeal pursuant to 28 U.S.C. § 1292(b) (1982), and staying the District Court's order denying class certification (App. Exhibit E) is reported as *Sanders v. Robinson Humphrey/American Express, Inc.*, [1986-87 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 92,880 (N.D. Ga. July 8, 1986).

The order of the Court of Appeals accepting the appeal pursuant to 28 U.S.C. § 1292(b) (1982) is not reported and is set forth in the Appendix as Exhibit F.

JURISDICTION

The judgment of the Court of Appeals was entered on September 15, 1987. (App. Exhibit A). Rehearing and rehearing *en banc* were denied by order dated October 21, 1987. (App. Exhibit B). The mandate of the Court of Appeals was stayed on November 17, 1987. (Appendix Exhibit C). Petitioner purports to invoke this Court's jurisdiction pursuant to 28 U.S.C. § 1254(1) (1982).

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[1] Citations herein to material printed in the Appendix appear as either "Appendix" or "(App. ___)." Such citations are to the Appendix to the Petition filed by petitioner on or about December 7, 1987.

STATUTES AND RULES INVOLVED

The statutes and rules involved in the case are Sections 11 and 12(2) of the Securities Act of 1933, 15 U.S.C. §§ 77k, 77*l*(2) (1982); Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b) (1982); Securities and Exchange Commission Rule 10b-5, 17 C.F.R. § 240.10b-5 (1987); Rule 23 of the Federal Rules of Civil Procedure; and 28 U.S.C. § 1292(b) (1982). (App. Exhibit G).

COUNTERSTATEMENT OF THE CASE

Background

The instant case represents but a small part of the litigation arising out of the debacle involving Petro-Lewis, and brokerage firms such as petitioner which assisted Petro-Lewis in its scheme.[2] Over a 14-year period, Petro-Lewis sold, through securities brokerage firms, in excess of three billion dollars ($3,000,000,000) in limited partnerships to approximately 180,000 people. Brokerage firms such as petitioner readily participated in perpetrating this massive fraudulent scheme for a very simple reason—greed. These firms earned huge commissions for selling these securities—commissions which greatly exceeded their normal commissions.

From 1970 through 1983, Petro-Lewis was the nation's largest seller of oil and natural gas "income funds". These income funds were sold as safe, secure, conservative investments. Petro-Lewis and petitioner lured new investors with enticements of stable annual returns of 12% or more earned by previous partnerships, and by the apparent liquidity provided by Petro-Lewis' pledge to repurchase any partnership interest tendered by investors.

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[2] This case arises out of the same facts and involves the same legal issues presented in companion cases before this Court, *Robinson-Humphrey/American Express, Inc. v. Glenn T. Sanders and Leslie D. Sanders*, Case No. 87-835, and *Paine Webber Group, Inc. v. Parker, et al.*, Case No. 87-836.

The method of operation was consistent during the entire period in question. Petro-Lewis formed a new partnership each month. Cash distributions to the limited partners, which were paid quarterly, began almost immediately after each partnership was formed and were to continue for 10 to 15 years or more until the wells were depleted. Funds to pay partnership distributions were supposed to come from profits realized from the sale of oil and gas produced by the partnership properties.

Crucial to the success of this marketing scheme was the apparent steady pattern of cash flow to the limited partners, commencing almost immediately after the formation of the partnerships. Petro-Lewis and petitioner touted this "regular, reasonably predictable pattern of distributions" in prospectuses for the partnerships and in other written material distributed to potential investors. *Sanders v. Robinson-Humphrey/American Express, Inc.*, 634 F.Supp. 1048, 1050 (N.D. Ga. 1986)(App. D-2).

Petitioner played an important role in the marketing of these programs, selling in excess of $50,000,000 of limited partnership interests to over 8,000 investors. Petitioner found these programs to be extremely lucrative since Petro-Lewis paid commissions at a rate which averaged 7%, far in excess of the normal commissions earned on the sale of stocks and bonds.

Petitioner's desire to sell Petro-Lewis units permeated its entire organization. The units were marketed and sold to retirees, pension and profit-sharing plans, and other investors who desired conservative investments. Petitioner and its brokers actively assisted Petro-Lewis in disseminating prospectuses and other documents which contained numerous omissions and misrepresentations. Petro-Lewis itself closely monitored the sales by petitioner's brokers, and gave prizes to those brokers who achieved certain sales levels. *Sanders*, 634 F.Supp. at 1055 (App. D-6 to 7).

However, unbeknownst to the investors and members of the class, the impression of financial strength and success created by Petro-Lewis and petitioner was wholly unfounded.

This impression was designed specifically to attract new investors, and to deter existing partners from exercising their redemption options. The truth was that, contrary to the impression conveyed to the public, by at least the beginning of 1981, Petro-Lewis and its partnerships were experiencing serious financial problems. Without continuing sales to new investors, Petro-Lewis would run out of money to fund its operations and pay cash distributions.

Petro-Lewis had paid premium prices for the partnership properties and had borrowed heavily from banks to help finance the acquisitions. The funds to repay those loans, like the cash distributions to the partners, were supposed to come from the profits generated by the sale of oil and gas produced by the partnership properties. However, the advent of the world oil glut and attendant reduction in oil and gas prices in the early 1980's—coupled with, among other things, increased operating costs, huge debt service requirements and competition from other petroleum investment programs—resulted in a reduction in cash flow from the partnership properties. These conditions put Petro-Lewis in a serious cash bind and jeopardized the partnership holdings.

In 1984, the Ponzi scheme collapsed. Petro-Lewis suspended its partnership syndication operations and sold almost one third of the oil and gas reserves held by the partnerships in order to achieve a one billion dollar ($1,000,000,000.00) reduction in bank debt. Petro-Lewis also cut distributions to limited partners, imposed a cap on redemptions of partnerships, and reduced the prices at which Petro-Lewis repurchased those interests to a fraction of previous levels. Investors learned for the first time that the reserves purchased with their capital contributions were worth only ⅓ to ½ of what the partnerships had paid for them. *Sanders,* 634 F.Supp. at 1054 (App. D-6).

Investors who retained their partnership interests held, until recently, units in a royalty trust, which was created as part of the complicated settlement of *In re: Petro-Lewis Securities Litigation,* [1984-85 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 91,899 (D.Colo. 1984), a class action against Petro-

Lewis, its officers and directors. The defendants in that case consented to class certification and a settlement less than six (6) months after the complaint was filed; however, the amount recovered, $23.5 million, was hardly sufficient to compensate the individuals who suffered such astronomical losses. Therefore, members of the class involved in the Colorado litigation expressly retained their rights to pursue their claims against the brokerage firms, including petitioner and other brokerage firms who had participated with Petro-Lewis in marketing the limited partnerships interests. Even taking into account the proceeds from the *Petro-Lewis* settlement, losses to the investors and members of the proposed class in this case have been enormous. *Sanders,* 634 F.Supp. at 1050, 1052 (App. D-4).

Course Of Proceedings And Disposition In The Courts Below

On March 6, 1985, respondents filed a Class Action Complaint (the "Complaint") against petitioner for violations of the federal securities laws and common law arising out of its participation in the scheme outlined above. The Complaint asserts claims against petitioner under Sections 11 and 12(2) of the Securities Act of 1933 (the "Securities Act"), 15 U.S.C. §§ 77k and 77*l*(2), Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act"), 15 U.S.C. § 78j(b), Rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5 (1987), and for common law fraud, fraudulent concealment, negligence and breach of fiduciary duty. The thrust of the Complaint is that petitioner violated these statutory and common law provisions: (1) by disseminating virtually identical prospectuses for the partnership programs during the class period which omitted materially adverse information concerning Petro-Lewis and its partnerships, and (2) by perpetrating a scheme and common course of conduct at the highest levels of petitioner's corporate management which had the purpose and effect of suppressing the truth about the precarious financial condition of Petro-Lewis and its partnership programs. *Kirkpatrick v. J. C. Bradford & Co.,* 827 F.2d 718, 721 (11th Cir. 1987) (App. A-5).

BEST

The Complaint contains more than thirty (30) pages of allegations that the prospectuses and other written documents disseminated by Petro-Lewis and petitioner were false and misleading. The Complaint alleges in excruciating detail the omissions and misrepresentations contained in the prospectuses. Significantly, all of the allegations set forth in respondents' Complaint were asserted by the Securities and Exchange Commission ("SEC") in a separate complaint filed against Petro-Lewis seven months after this litigation began.

Among these allegations are the following:

1. The prospectuses failed to disclose the risks inherent in purchasing Petro-Lewis limited partnership interests;

2. The prospectuses failed to disclose the excessive leveraging of the partnerships;

3. The prospectuses failed to disclose that Petro-Lewis engaged in a pattern of "propping up" cash distributions to the partnerships by using borrowed funds. In fact, respondents received documents during the discovery process which show that the cash distributions to the partnerships had been supported by up to forty percent (40%) through the use of borrowed funds, a material fact which respondents allege was not disclosed to class members;

4. The prospectuses failed to disclose that distributions were being inflated in order to ensure that sales continued;

5. The prospectuses failed to disclose that substantial tax benefits expected to be received by class members were likely to be disallowed;

6. The prospectuses failed to disclose that declines in the price of oil would and did make it impossible to adequately service the partnerships' debt;

7. The prospectuses failed to disclose that due to Petro-Lewis' policy of borrowing to make distributions, a substantial risk existed that, contrary to the statements in the prospectuses, no funds would be available to repurchase interests;

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8. The prospectuses failed to adequately disclose that Petro-Lewis utilized improper or highly questionable accounting practices and policies; and

9. The documents disseminated by Petro-Lewis and petitioner failed to disclose that extensive leveraging created the risk of forced liquidation of partnership assets.

The conspiracy and common course of conduct which respondents' Complaint alleges was perpetrated at the highest levels of petitioner's corporate management. Respondents do not complain of, nor have they ever asserted any claim based upon, any oral statements made to them or any other class member by any individual employed by petitioner. *Kirkpatrick*, 827 F.2d at 721, 724 (App. A-5, 10 to 11). *See also Sanders*, 634 F.Supp. at 1053-54 (App. D-6 to 9).

The hearing on respondents' motion for class certification took place on February 27, 1986 following briefing and discovery. In its papers opposing the motion, petitioner consistently mischaracterized respondents' case to the District Court, arguing that it was one based solely on "oral misrepresentations." This self-serving characterization was reached only by totally ignoring respondents' Complaint in this case, and through a gross distortion of the record which had been developed on the class issue.[3]

In an order dated March 27, 1986, the District Court denied respondents' motion for class certification. The District Court refused to give separate consideration to class treatment of respondents' Securities Act claims. With respect to respondents' Exchange Act claims, the District Court specifically found that the case "clearly" satisfied the "commonality" requirement of Rule 23(a)(2) of the Federal Rules of Civil Procedure. The District Court held that all members of the class shared numerous common legal and factual issues relating to the prospectuses and petitioner's persistent failure to disclose

[3] Respondents made detailed written submissions to the District Court on the class motion prior to the hearing. This included, in addition to extensive briefs, numerous items of documentary evidence and other factual material.

material facts concerning the risks inherent in the Petro-Lewis programs. *Sanders*, 634 F.Supp. at 1056 (App. D-13). Similarly, the District Court found that the "typicality" requirement of Rule 23(a)(3) was easily satisfied in the case in light of the allegations that petitioner had engaged in a common course of conduct which affected each member of the class in the same manner. *Sanders*, 634 F.Supp. at 1057 (App. D-15).

When it reached the "predominance" element of Rule 23(b)(3), however, the District Court took an entirely different view of the case. In a totally inexplicable reversal of position, the District Court disregarded its own findings on "commonality" and "typicality". The District Court inconsistently ruled that respondents' Section 10(b) and Rule 10b-5 claims were grounded solely upon "oral misrepresentations" between members of the class and their individual brokers—a formulation of the case which respondents had neither pleaded nor intended to prove. The District Court adopted that characterization despite the absence from the Complaint of any allegation that respondents' claims were grounded on any such oral statements. Having thus recast the case, the District Court ruled that class certification of the Section 10(b) and Rule 10b-5 claims would be appropriate only if respondents were able to demonstrate that petitioner had engaged in a uniform "presentation" or standardized "sales pitch" directed to each and every member of the class. Finding the "evidence" on this issue to be deficient, the District Court refused to grant class action status to respondents' Exchange Act claims. *Sanders*, 634 F.Supp. at 1061-63 (App. D-23 to 27).

The District Court also ruled that the mere possibility that each member of the class might have to prove his or her individual reliance constituted a *per se* bar to class certification. *Sanders*, 634 F.Supp. at 1061, 1063 (App. D-23, 27). The District Court, therefore, focused its inquiry on whether reliance may be presumed under the "fraud on the market" theory adopted in *Shores v. Sklar*, 647 F.2d 462 (5th Cir. 1981) (*en banc*), *cert. denied*, 459 U.S. 1102 (1983). Ignoring numerous paragraphs of respondents' Complaint which contain this *precise* allegation, the District Court held that respondents "*do not*

allege that the securities would not have been sold had the misrepresentations not been present"—a necessary predicate to the *Shores* presumption. *Sanders*, 634 F.Supp. at 1063 (App. D-28) (emphasis added). Based on this and its other findings, the District Court denied class certification.

Respondents filed a timely motion for reconsideration which, in an order dated July 8, 1986, the District Court also denied. *Sanders*, [1986-87 Transfer Binder] ¶ 92,880 at 94,267 (App. Exhibit E). As they had done previously, respondents pointed out, in their motion for reconsideration, that they had, indeed, clearly and unambiguously alleged in their Complaint that "but for" the presence of the misrepresentations and omissions, the partnership interests could not have been sold. Apparently mindful of its previous erroneous ruling on this issue, the District Court, in its July 8th order, shifted its analysis to an evaluation of the "support" for that allegation. The District Court conducted a selective analysis of what it considered to be the "evidence" for that allegation and determined that it was insufficient to support the theory. *Sanders*, [1986-87 Transfer Binder] ¶ 92,880 at 94,271-72 (App. E-9 to 11). However, the District Court specifically found that the issue of class certification involved several controlling questions of law about which substantial grounds existed for differences of opinion and that an immediate appeal from its two orders would materially advance the ultimate termination of the litigation. *Sanders*, [1986-87 Transfer Binder] ¶ 92,880 at 92,274-75 (App. E-17 to 19). Accordingly, the District Court certified the class issue for interlocutory appeal pursuant to 28 U.S.C. § 1292(b) (1982). The Eleventh Circuit Court of Appeals accepted the appeal in an order dated August 21, 1986 (App. Exhibit F).

In a unanimous opinion, the Court of Appeals reversed the denial of class certification with respect to respondents' federal securities law claims. The Court of Appeals ruled that the District Court had erred in refusing to give any consideration whatsoever to possible class treatment of respondents' claims under Sections 11 and 12(2) of the Securities Act. *Kirkpatrick*, 827 F.2d at 725-26 (App. A-12 to 13).

Turning to respondents' Section 10(b) and Rule 10b-5 claims, the Court of Appeals observed that the District Court's entire analysis of the "predominance" issue was "based directly on [its] interpretation of the substance of the plaintiffs' claims." *Kirkpatrick*, 827 F.2d at 721 (App. A-4). Accordingly, the Eleventh Circuit reviewed respondents' Complaint to determine whether the District Court had properly construed those claims. The Court of Appeals concluded that the District Court had not. The Eleventh Circuit unanimously held that the District Court had "mischaracterized" the case as one involving "primarily individualized oral representations rather than a common scheme by the defendants toward the plaintiff purchasers." *Kirkpatrick*, 827 F.2d at 722, 725 (App. A-6, 11). Having placed the case in its proper context, the Court of Appeals carefully reviewed the entire record in the case, and determined that the "predominance" requirement of Rule 23(b)(3) was easily satisfied. *Kirkpatrick*, 827 F.2d at 724 (App. A-10). The Eleventh Circuit, following a long and unbroken line of authority, held that "[i]n view of the overwhelming number of common factual and legal issues presented by plaintiffs' misrepresentation claims, . . . the mere presence of the factual issue of individual reliance could not render the claims unsuitable for class treatment." *Kirkpatrick*, 827 F.2d at 724-25 (App. A-11). The Eleventh Circuit also held that the case fell squarely within the principles announced in *Shores v. Sklar*, and that respondents were entitled to a presumption of reliance afforded by the "fraud on the market" theory recognized in that case. In so doing, the Court of Appeals ruled that the District Court could not, as it had done, base its findings on class certification "*upon nothing other*" than the District Court's assessment of the likelihood of success on the merits of respondents' claims. *Kirkpatrick*, 827 F.2d at 723 (App. A-7)(emphasis added).

Having corrected the numerous legal and factual errors which plagued the District Court's orders, the Court of Appeals remanded the class issue to the District Court for application of the correct standards. *Kirkpatrick*, 827 F.2d at 720, 728 (App. A-2, 17).

SUMMARY OF ARGUMENT

The issues raised in the Petition present no novel or unique questions of constitutional or statutory interpretation worthy of review by this Court. The decision of the Court of Appeals is firmly rooted in the precedents of this Court, follows a long and unbroken line of authority in the Eleventh Circuit, and is fully consistent with the case law in other Circuits. The alleged "conflict" which petitioner strives to create is nonexistent.

REASONS FOR DENYING THE PETITION

I.

THE ISSUES RAISED IN THE PETITION ARE NOT RIPE FOR DETERMINATION WITH RESPECT TO ALL OF THE QUESTIONS PRESENTED FOR REVIEW

The Court of Appeals neither granted nor denied class certification. Rather, the Eleventh Circuit remanded the class issue to the District Court for further proceedings consistent with its decision. Thus, the class motion remains undecided. Under these circumstances, it is unnecessary for this Court to exercise its certiorari jurisdiction at this time to render what essentially would be an advisory opinion.

In *Brotherhood of Locomotive Firemen and Enginemen v. Bangor & Aroostook R.R. Co.*, 389 U.S. 327 (1967), the Court denied a petition for writ of certiorari where the court of appeals had remanded the case to the district court for further proceedings. In *Brotherhood*, the district court had issued a temporary restraining order against a union prohibiting a strike. The union nevertheless went on strike, and the district court entered contempt orders, imposing substantial fines for alleged violations of its restraining order. On appeal, the court of appeals ruled on many of the legal issues presented to it, but remanded the case to the district court to determine whether there had been substantial compliance with the restraining order and, if not, whether any such violation of the order had been deliberate and flagrant. *Bangor & Aroostook R.R. Co. v. Brotherhood of Locomotive Firemen and Enginemen*, 380 F.2d

570 (D.C.Cir. 1967). The union sought certiorari to review the adverse rulings made by the court of appeals. This Court, noting that the court of appeals had remanded the case, held the issues were "not yet ripe for review by this Court," and denied the petition. 389 U.S. at 328.

Just as the court of appeals in *Brotherhood* did not make findings on critical issues but, rather, remanded the case to the district court for further proceedings, so the Eleventh Circuit here did not certify a plaintiff class but, rather, remanded the case to the District Court for further findings. The issues involved in this case, as in *Brotherhood*, simply are "not yet ripe for review."

There is no particular exigency which would attend the denial of certiorari in this case. Petitioner will be free to challenge, as part of the normal appellate process after final judgment, any class which the District Court ultimately might certify in this case. In the interim, numerous developments might occur which could significantly alter or entirely moot the issues raised in the Petition. For example, the District Court might certify a class different from the class pleaded in respondents' Complaint or refuse to certify the Securities Act claims. The District Court also may subsequently alter or amend any certification order which it might enter in this case. *See* Fed.R.Civ.P. 23(c)(1) (district court retains authority to alter or amend a class order until "a decision on the merits"). The jury may return a verdict in favor of petitioner on the merits of respondents' claims, thereby effectively mooting all of the issues raised in the Petition. Petitioner has stretched the truth in its attempt to convince this Court to exercise its jurisdiction in this case at this time. A perfect example is petitioner's argument with respect to the Eleventh Circuit's handling of the adequacy of respondents as class representatives. Petitioner claims:

> The District Court expressly found, and the Court of Appeals did not question, that respondents would not adequately represent the interests of other class members . . . .

(Petition, p. 17). In fact, the Eleventh Circuit found that the District Court had applied an incorrect standard in determining the "adequacy" requirement of Rule 23(a)(4) (App. A-17). The Eleventh Circuit specifically refused to conduct an independent application of the correct standard in this case but remanded to the District Court for a factual determination using the correct legal standard—a standard which is virtually identical to that adopted in every other circuit.

Exercise by this Court of jurisdiction at this time is inappropriate. The issues simply are entirely too distant and speculative to warrant review at this time.

As the Court held almost a century ago in *American Construction Co. v. Jacksonville, Tampa & Key West Ry. Co.*, 148 U.S. 372 (1893):

> Whether an interlocutory order may be separately reviewed by the appellate court in the progress of the suit, or only after and together with the final decree, is matter of procedure rather than of substantive right; and *many orders made in the progress of a suit become quite unimportant by reason of the final result or of intervening matters.* Clearly, therefore, *this court should not issue a writ of certiorari to review a decree of the circuit court of appeals on appeal from an interlocutory order, unless it is necessary to prevent extraordinary inconvenience and embarrassment in the conduct of the cause.*

Id. at 384 (emphasis added). The Court reaffirmed these principles two decades later in *Hamilton-Brown Shoe Co. v. Wolf Bros. & Co.*, 240 U.S. 251 (1916), when it stated:

> [Certiorari] is a jurisdiction to be exercised sparingly, and only in cases of peculiar gravity and general importance, or in order to secure uniformity of decision .... *And except in extraordinary cases, the writ is not issued until final decree* .... The decree that was sought to be reviewed by certiorari at complainant's instance *was not a final one, a fact that of itself alone furnished sufficient ground for the denial of the application.* ...

Id. at 258 (emphasis added)(citations omitted). *See also* Supreme Court Rule 17.1. Here, review of the class issue should await not just a ruling on the class motion itself, but final judgment in this case.

There is another, equally compelling, reason for denying the Petition. The centerpiece of petitioner's argument unquestionably is its frontal assault on the "fraud on the market" theory enunciated in *Shores v. Sklar.* While that theory may have some bearing on some of respondents' claims, it is undisputed that the "fraud on the market" theory is not implicated at all with respect to several of respondents' other claims. For example, the Court of Appeals ruled that the District Court "improperly found that the plaintiffs' Rule 10b-5(2) misrepresentation claims were not suited for class treatment." *Kirkpatrick*, 827 F.2d at 724 (App. A-10). In so doing, the Court of Appeals held that "the mere presence of the factual issue of individual reliance could not render the claims unsuitable for class treatment." *Kirkpatrick*, 827 F.2d at 724-25 (App. A-11).[4] Thus, respondents need not rely on the presumption of reliance afforded by the "fraud on the market"

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[4] This principle has received such widespread and uniform acceptance by the Circuits that it is no longer subject to serious dispute. *See, e.g., Eisenberg v. Gagnon*, 766 F.2d 770, 786 (3d Cir.), *cert. denied*, 106 S.Ct. 342 (1985); *Blackie v. Barrack*, 524 F.2d 891, 902 (9th Cir. 1975), *cert. denied*, 429 U.S. 816 (1976); *Green v. Wolf Corp.*, 406 F.2d 291, 301 (2d Cir. 1968), *cert. denied*, 395 U.S. 977 (1969). As the Second Circuit observed in *Green:*

> Wolf earnestly argues that each person injured must show that he personally relied on the misrepresentations in order to recover and thus any common issues of misrepresentations do not predominate over the individual questions of reliance. Even if Wolf is correct in its assertion of the need for proof of reliance, and we express no views on that issue, we must still reject the argument. Carried to its logical end, it would negate any attempted class action under Rule 10b-5, since as the District Courts have recognized, reliance is an issue lurking in every 10b-5 action.

406 F.2d at 301. *Accord, In re Home-Stake Production Co. Securities Litigation*, 76 F.R.D. 351, 372 (N.D. Okla. 1977); *Sharp v. Coopers & Lybrand*, 70 F.R.D. 544, 547-48 (E.D. Pa. 1976); *Vernon J. Rockler v. Graphic Enterprises, Inc.*, 52 F.R.D. 355, 345-46 (D. Minn. 1971).

theory for class certification of their Rule 10b-5(2) misrepresentation claims.

In summary, the District Court, on remand, must reconsider the issue of class certification irrespective of the outcome of the issues raised in the Petition. Under these circumstances, granting the writ will serve merely to delay the resolution of this case without any concomitant contribution to the preservation of judicial resources. To the contrary, the judicial process will be ill-served by such piecemeal, fragmented litigation.

II.

THE DECISION OF THE COURT OF APPEALS IS FIRMLY ROOTED IN WELL-SETTLED PRINCIPLES OF LAW AND PROCEDURE AND IS FULLY CONSISTENT WITH EXISTING PRECEDENT

The Court of Appeals—far from according blind deference to respondents' Complaint, as petitioner suggests—merely held that the District Court could not disregard respondents' Complaint in its entirety and unilaterally reformulate respondents' case in a manner which they neither pleaded nor intended to prove. The Eleventh Circuit adopted a view of the case which *the District Court itself* had adopted in analyzing the "commonality" and "typicality" requirements of Rule 23—one grounded on a common course of fraudulent conduct which affected each member of the class in the same manner, and involving widely distributed uniform written material. The Court of Appeals held that the evidence presented both prior to and during the class certification hearing, *viewed in its proper context,* supported certification of the Section 10(b) and Rule 10b-5 claims. The Court of Appeals' decision is legally correct, factually sound, and does not merit review by this Court. One need only read respondents' Complaint (something which the District Court stated it was not required to do) to reach the same conclusion.

Petitioner has only itself to blame for misleading the District Court through its persistent mischaracterizations of respondents' case. Such tactics frequently are employed by

those who would deny any relief to a class of defrauded investors. Typical is *Shankroff v. Advest, Inc.*, 112 F.R.D. 190 (S.D.N.Y. 1986), a case involving another brokerage firm which sold the Petro-Lewis partnerships. The *Shankroff* court rejected the brokerage firm's attempt, like petitioner here, to mischaracterize the issues as highly individual in nature. The court held that the complaint alleged that the brokerage firm engaged in a course of conduct designed to encourage investment in Petro-Lewis while failing to disclose the "deplorable" financial condition of Petro-Lewis. 112 F.R.D. at 193. *Accord, In re Baldwin-United Corporation Litigation*, MDL No. 581, M 21-35 (CLB) (S.D.N.Y., June 27, 1986 Memorandum Decision Granting Class Certification (a copy of which is appended hereto as Respondents' Appendix A)).

As the Eleventh Circuit specifically found, the focus of this case is on the prospectuses and other written material distributed to members of the class and on the fraudulent conduct of petitioner's senior management, *not* on any ancillary oral statements made by individual brokers employed by petitioner to their clients.[5] Under such circumstances, courts have uniformly held that mere presence of oral statements will not render individual questions of reliance predominant over the common issues of fraud and materiality. *See, e.g., Kennedy v. Tallant*, 710 F.2d 711, 717-18 (11th Cir. 1983)("The substance of the oral representations made by the various salesmen is not an issue in this suit."); *Esplin v. Hirschi*, 402 F.2d 94, 97 (10th Cir. 1968), *cert. denied*, 394 U.S. 928 (1969) ("undoubtedly the possibility exists that there will be questions of individual oral misrepresentations to each of the potential plaintiffs," but "having alleged . . . that there was omissions and half truths common to all purchasers . . . it is apparent that the issue of liability . . . was to be the same as to all purchasers"); *Arthur Young & Co. v. United States District Court*, 549 F.2d 686, 695

[5] The Eleventh Circuit also specifically found that the record in this case was devoid of any evidence that class members were even exposed to differing oral communications, let alone that any such communications "varied materially from the misleading information alleged to have been disseminated generally as a result of the defendants' common schemes." *Kirkpatrick*, 827 F.2d at 724 (App. A-10). This is uncontroverted.

(9th Cir.) *cert. denied,* 434 U.S. 829 (1977) (alleged reliance on oral statements was of "questionable evidentiary significance for purposes of making a Rule 23 determination" in cases involving primarily written misrepresentations); *Eisenberg v. Gagnon,* 766 F.2d 770, 786 (3d Cir.), *cert. denied,* 106 S.Ct. 342 (1985) (denial of class certification under similar facts was an "abuse of discretion"); *In re Home-Stake Production Co. Securities Litigation,* 76 F.R.D. 351, 369-73 (N.D. Okla. 1977) (possible variations in oral statements made to limited partners in oil and gas investment programs did not defeat class certification when a fraudulent prospectus was also the basis of plaintiff's claim).

These courts have adopted a common-sense approach, and recognize that it is a rare securities transaction which is not accompanied by some type of oral communication between an investor and his or her broker. Adoption of a *per se* bar to class certification whenever a securities transaction involves oral communications—the very position advocated by petitioner and adopted by the District Court here—would totally eviscerate the class action device in the securities context. It is undoubtedly for this reason that the courts have consistently rejected such an approach, and that the Eleventh Circuit recognized in this case that respondents' claims "essentially involve allegations that the defendants 'committed the same unlawful acts in the same method against the entire class.'" (App. A-10) (citations omitted).

In this connection, petitioner apparently refuses to recognize the difference between "oral representations" and "oral *mis*representations." The former may be entirely consistent with the written materials and their mere presence in a case, as the Eleventh Circuit found here and as the cases cited previously uniformly hold, will not defeat certification. Oral *mis*representations, by contrast, may give rise to liability under the federal securities laws, and present a problematic situation for class certification, *if—but only if—the class' claims are grounded on those oral misstatements.* In those types of cases, the plaintiff must come forward with evidence of a standardized sales pitch in order to satisfy the requisite "commonality" and "predominance" elements of Rule 23. That is not *this* case.

III.

THE DECISION OF THE COURT OF APPEALS FALLS SQUARELY WITHIN THE HOLDING OF *SHORES v. SKLAR* AND THE UNBROKEN LINE OF AUTHORITY WHICH HAS FOLLOWED IN ITS WAKE

The Court of Appeals correctly held, as has every other court which addressed the issue,[6] that a plaintiff alleging fraud under Rule 10b-5 may, in circumstances where it is alleged that securities could not have been marketed "but for" the fraud, invoke a rebuttable presumption of reliance upon the integrity of the marketplace. *Kirkpatrick*, 827 F.2d at 722-23 (App. A-6 to 7), citing *Shores v. Sklar, supra.*[7] The fraud on the market theory as enunciated by the Eleventh Circuit is consistent with other circuits and clearly furthers the purposes of the securities laws. As this Court held in *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976), the securities acts were designed to protect investors against fraud and to promote ethical standards of honesty and fair dealing.

Reliance is generally part of the logical chain needed to establish an element of a 10b-5 claim: that a defendant's misrepresentation or omission in fact caused the plaintiff's injury. *See List v Fashion Park, Inc.*, 340 F.2d 457, 462 (2d Cir.), *cert. denied*, 382 U.S. 811 (1965). Although the requirement is easily met by showing the plaintiff's actual subjective reliance on the defendant's misstatement (*see* 3 L.

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[6] *See, e.g., T.J. Raney & Sons, Inc. v. Fort Cobb Oklahoma Irrigation Fuel Authority*, 717 F.2d 1330, 1333 (10th Cir. 1983), *cert. denied*, 465 U.S. 1026 (1984); *Shores v. Sklar, supra; Arthur Young & Co. v. United States District Court*, 549 F.2d 686, 695 (9th Cir.), *cert. denied*, 434 U.S. 829 (1977); *Rose v. Arkansas Valley Environmental & Utility Authority*, 562 F.Supp. 1180, 1201-03 (W.D. Mo. 1983); *Frankel v. Wyllie & Thornhill, Inc.*, 537 F.Supp. 730, 735-37 (W.D. Va. 1982); *Dekro v. Stern Bros. & Co.*, 540 F.Supp. 406, 410-11 (W.D. Mo. 1982). *See also* Note, *Fraud on the Market—An Emerging Theory Of Recovery Under SEC Rule 10b-5*, 50 Geo. Wash. L. Rev. 627, 645-55 (1982).

[7] The Eleventh Circuit, in the *en banc* decision *Bonner v. City of Prichard*, 661 F.2d 1206 (11th Cir. 1981), adopted as precedent the decisions of the former Fifth Circuit, including *Shores*, rendered prior to October 1, 1981.

Loss, *Securities Regulation*, at 1430-32 (2d ed. 1961)), courts have held that proof of such direct reliance is not necessary in certain cases, including those alleging a *Shores*-type "fraud on the market."

The "fraud on the market" theory recognized in *Shores* (and reaffirmed by the Eleventh Circuit here) is grounded on the premise that "[t]he securities laws allow an investor to rely on the integrity of the market to the extent that the securities it offers to him for purchase are entitled to be in the marketplace." *Shores*, 647 F.2d at 471. Under *Shores*, the requisite causation is provided by proof that "securities not traded on the open market could not have been issued but for a fraudulent scheme by the defendants." *Kirkpatrick*, 827 F.2d at 722 (App. A-7), *citing Shores*, 647 F.2d at 469. Allegations to that effect allow a rebuttable presumption that investors who purchased the securities and relied on the integrity of the market were harmed by the defendant's fraud.

The logic underlying the theory is manifest. If securities could not have been marketed but for a fraudulent scheme, it follows that an investor satisfies the requisite causal link by evidence that he or she purchased the securities in reliance, in whole or in part, on the integrity of the market. Indeed, as the Eleventh Circuit noted here, recognition of the "fraud on the market" theory is as compelling in a *Shores*-type case as it is in a so-called "open market" [8] context:

> A *Shores* fraud-on-the-market claim thus is especially suited for class action treatment, as it makes virtually

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[8] See *Basic Inc. v. Levinson*, 107 S.Ct. 1284 (1987), *granting cert. to*, 786 F.2d 741 (6th Cir. 1986). *See also Peil v. Speiser*, 806 F.2d 1154 (3d Cir. 1986); *Harris v. Union Electric Co.*, 787 F.2d 355, 367 & n. 9 (8th Cir. 1986), *cert. denied*, No. 85-2036 (Oct. 6, 1986); *Lipton v. Documation, Inc.*, 734 F.2d 740 (11th Cir. 1984), *cert. denied*, 469 U.S. 132 (1985); *T.J. Raney & Sons, Inc. v. Fort Cobb Oklahoma Irrigation Fuel Authority*, 717 F.2d 1330 (10th Cir. 1983), *cert. denied*, 465 U.S. 1026 (1984); *Panzirer v. Wolf*, 663 F.2d 365 (2d Cir. 1981), *vacated as moot after cert. granted*, 459 U.S. 1027 (1982); *Ross v. A.H. Robins Co.*, 607 F.2d 545, 553 (2d Cir. 1979), *cert. denied*, 446 U.S. 946 (1980); *Blackie v. Barrack*, 524 F.2d 891 (9th Cir. 1975), *cert. denied*, 429 U.S. 816 (1976).

> irrelevant the possibility that the various purchasers may have relied on different representations regarding the desirability of the particular security in question; all have relied on the integrity of the market in the but-for sense required by *Shores*.

Kirkpatrick, 827 F.2d at 718 (App. A-9)(footnote omitted). A similar view was expressed by the Ninth Circuit in *Arthur Young & Co. v. United States District Court, supra*, when it observed:

> Just as the open market purchaser relies on the integrity of the market and the price of the security traded on the open market to reflect the true value of securities in which he invests, so the purchaser of an original issue security relies, at least indirectly, on the integrity of the regulatory process and the truth of any representations made to the appropriate agencies and the investors at the time of the original issue.

549 F.2d at 695.

Courts have similarly accepted the common-sense observation that most investors rely on the integrity of the market in making trading decisions. As one court has observed: "It is hard to imagine that there ever is a buyer or seller who does not rely on market integrity. Who would knowingly roll the dice in a crooked crap game?" *Schlanger v. Four-Phase Systems, Inc.*, 555 F.Supp. 535, 538 (S.D.N.Y. 1982). The fact that persons invest in the market at all is evidence that they rely on the assumption "that the market is not being manipulated as a result of anybody's false statement or misleading omission." *Id.*

Respondents clearly alleged that the Petro-Lewis securities could not have been marketed "but for" the fraudulent scheme, and respondents came forward with uncontroverted evidence that they relied on the integrity of the market when they made their purchases. No more is required at the class certification stage.

Where, as here, material information is *not* "fully disclosed," investors are *not* "told the truth" about the security and, because of the foregoing, investors are *not* able to make an

"informed" investment decision, liability should and does attach under Rule 10b-5. If those same investors are successful in proving at trial that full and complete disclosure of all material information would have prevented the securities from being sold in the first place (i.e., rendered them "unmarketable"), and that petitioner participated in a scheme to suppress that information, the investors have proven a violation of Rule 10b-5(1) and (3). *See Shores*, 649 F.2d at 468-69. Among the items of evidence in this case, for example, which will be offered at trial are that critical parties to the offerings would not have participated in the syndications had the truth been known about the investments, and that insufficient funds would have been raised from subscriptions to purchase the oil reserves which constituted the partnership assets. Just as fraud can interfere with the market's pricing mechanism, it can also disrupt the issuance of "new" securities.

Critics of the *Shores* decision—including petitioner here—refer to disclaimers issued by the SEC that warn investors not to rely on the qualitative soundness of any security. This position miscontrues the remedial nature of the federal securities laws and is in conflict with the securities acts' objectives of full disclosure and investor protection. Although the SEC does not guarantee or pass judgment upon the qualitative soundness of particular securities, it would be fallacious to assume that investors are left unprotected against fraud in the issuance of those securities. The purpose of the SEC's disclaimers is to insulate the Commission against civil liability from disgruntled investors who have made poor investment decisions. Permitting an injured investor to compel the wrongdoer to compensate for the investor's losses does not interfere with that purpose and therefore should not be precluded by the disclaimers. *See* Note, *Fraud On The Market—An Emerging Theory of Recovery Under SEC Rule 10b-5*, 50 Geo. Wash. L. Rev. 627, 652-53 (1982).

Petitioner engages in a specious argument in its attempt to convince this Court that the decision of the Eleventh Circuit conflicts with other jurisdictions. Petitioner claims that the Eleventh Circuit, through the use of the terms "fraudulently marketed" at one point in its opinion, has changed the require-

ments for a *Shores*-type "fraud on the market" claim. (Petition, p. 11-12). Petitioner ignores the clear statement of the Eleventh Circuit:

> Because the Petro-Lewis shares were not traded on the open market, we need not now consider the appropriateness of class certification of traditional fraud-on-the-market claims involving securities that are openly traded. We concluded however, that where as here, a complaint alleges that a security not traded on the open market could not have been issued but for the fraud of the defendants, class action treatment is not precluded by the possibility that some purchasers, including the named plaintiffs, might have relied on factors other than the integrity of the market. (App. A-8).

Despite petitioner's misstatement of the Eleventh Circuit's decision, the opinion of the Eleventh Circuit is squarely on point with all other circuits which have considered the issue.

CONCLUSION

For the foregoing reasons, the Petition for Writ of Certiorari to review the decision of the United States Court of Appeals for the Eleventh Circuit should be denied.

Dated: Atlanta, Georgia
January 6, 1988

Respectfully submitted,

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APPENDIX A

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

IN RE BALDWIN-UNITED CORPORATION LITIGATION

MDL 581
M 21-35 (CLB)

MEMORANDUM DECISION
[Class Certification]

This Document Relates To:

ALFRED LINTON and JEROME W. EICHELSBACHER,
Plaintiffs,

-against-

SHEARSON LEHMAN/AMERICAN EXPRESS, INC., *et al.*,
Defendants.

83 Civ. 8476 (CLB)

VINCENT ERTI, *et al.*,
Plaintiffs,

-against-

PAINEWEBBER JACKSON & CURTIS, INC., *et al.*,
Defendants.

83 Civ. 9085 (CLB)

(caption continues)

(caption continued)

OSCAR J. WOODS,
Plaintiff,

-against-

W.H. NEWBOLD'S SONS & CO., INC., *et al.*
Defendants.

84 Civ. 2235 (CLB)

STEVEN A. PEREL,
Plaintiff,

-against-

ROTAN MOSLE, INC., *et al.*,
Defendants.

84 Civ. 8879 (CLB)

Brieant, J.

By motion fully argued and submitted on March 7, 1986, plaintiffs in this multidistrict litigation seek class certification pursuant to Rule 23, F.R.Civ.P., in each of the above-captioned four actions, which have been consolidated in this Court by transfer orders on the Judicial Panel on Multidistrict Litigation. Familiarity of the reader with all prior proceedings in this litigation is assumed, although the Court directs special attention to its decision *In Re Baldwin-United Corp.*, 105 F.R.D. 475 (S.D.N.Y. 1984), in which the Court certified tentative classes in fourteen related cases against different defendants on similar claims, for the purpose of settlement. Subsequently, a total of twenty-four consolidated class actions against that many broker-dealer defendants in the Baldwin-United securities litigation were certified and each was settled.

Plaintiffs in these four remaining actions allege that the defendant broker-dealers and Planco, Inc. engaged in a common course of fraudulent conduct in omitting material information in connection with their sales of certain investment contracts to the plaintiffs. These contracts, known as single

premium deferred annuities (SPDAs), were issued from 1979 to 1983 by two insurance subsidiaries of Baldwin-United and were marketed to the public nationwide by various means, including sale through broker-dealers such as the defendants in these four actions. In 1983, the two issuing insurance companies and four other subsidiaries that reinsured the SPDAs were placed in rehabilitation, and the parent corporation, Baldwin-United, entered bankruptcy. Thereafter, SPDA purchasers, including the class plaintiffs herein, commenced the federal civil actions that eventually were consolidated into this multidistrict litigation.

Jurisdiction is conferred over the federal law claims by Section 22 of the Securities Act of 1933 ("1933 Act"), 15 U.S.C. § 77(v), Section 27 of the Securities Exchange Act of 1934 ("1934 Act"), 15 U.S.C. § 78aa, and Section 4 of the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. § 1964. The Court is likewise empowered to hear the state statutory and common law claims pleaded by virtue of diversity of citizenship and under principles of pendent jurisdiction.

The amended consolidated complaints in the *Linton*, *Erti* and *Woods* actions and the complaint in *Perel* each recite nine separately denominated claims for relief alleging violations of Sections 5, 12(1) of the Act, 15 U.S.C. § 78j(b) and Rule 10b-5 promulgated thereunder, and Section 1962(c) of RICO, as well as common law fraud and deceit and violations of state securities, consumer and fiduciary responsibility laws. The plaintiffs also assert claims premised on common law negligence, breach of contract and breach of fiduciary duty against all defendants except Planco, Inc. ("Planco"). Except for variations in the pleadings to account for facts peculiar to each plaintiff, the complaints are identical in all respects pertinent to these class certification motions. Therefore, the Court will not distinguish among them when examining their suitability for class certification, except as may be required to consider specific, fact-oriented arguments raised by a particular broker-dealer that call for individualized analysis.

Numerosity

In order to qualify for class action treatment, plaintiff must demonstrate that each of the four prerequisites set forth in Rule 23(a) has been satisfied and, in addition, that at least one of the factors described in Rule 23(b) is present. The first requirement, that the classes be so numerous that joinder of all the aggrieved individuals would be impracticable, is not contested here. Over several years, each broker-dealer sold SPDAs having an aggregate face value well in excess of a million dollars to purchasers throughout the country. The identity and exact number of prospective class members are ascertainable from defendants' records and those of the state rehabilitators of the issuers, and it is reasonable to conclude in view of the magnitude of this marketing effort that the number of affected persons would justify class certification.

Commonality

The second requirement, commonality, is more problematic. Under Rule 23(a)(2), plaintiffs must show that common questions of law and fact susceptible to class treatment predominate among the putative class members' claims. The gravamen of plaintiffs' complaints is that the defendants, in connection with their business of analyzing investment opportunities and providing financial services to clients, each engaged in a similar unified course of conduct to promote and sell Baldwin-United's SPDAs to the public without disclosing that the issuer was experiencing financial and regulatory difficulties. Plaintiffs contend that the defendants, at the corporate, policy making level, knew or recklessly disregarded evidence of Baldwin-United's precarious financial condition and that they elected to implement or maintain standardized marketing practices that concealed the true investment risks of the SPDAs. Those practices, plaintiffs allege, emphasized the safety, liquidity and promising investment aspects of the SPDAs even though information available to the defendants foretold Baldwin-United's collapse. Plaintiffs contend that the defendants' failure to investigate and ascertain the solidity of the SPDAs' financial backing, their practice of using uniformly deceptive promotional materials to solicit purchases, and their

failure or refusal to disclose the material omissions and half-truths embodied in their marketing strategy together caused SPDA holders to sustain substantial injury when their investments deteriorated.

The broker-dealers, for their part, deny that common issues of law and fact predominate. They maintain that the core issues submitted by plaintiffs in their complaints turn largely on oral rather than written representations, or on non-uniform documents that will require greater investigation and analysis of individual facts than class treatment will allow. For example, defendants assert, the threshold issue—whether the SPDAs are in fact securities—invites inquiry into the manner in which the SPDAs were sold and how they were described to prospective investors. Similarly, allegations of statutory and common law fraud would require the Court to make findings as to the parties' state of mind, the information disclosed, and also the fluctuating fortunes of Baldwin as of the time a particular investor made his or her purchase. The defendants therefore conclude that the highly individualized character of these transactions, affecting some 50,000 investors, makes class certification inappropriate.

This Court disagrees. The nub of plaintiffs' claims is that material information was withheld from the entire putative class in each action, either by written or oral communication. Essentially, this is a course of conduct case, which as pled satisfies the commonality requirement of Rule 23, F.R.Civ.P. *See, Green* v. *Wolf Corp.*, 406 F.2d 291, 300 (2d Cir. 1968), *cert. denied*, 395 U.S. 977 (1969). Although their circumstances may vary slightly, the class members are united in attempting to establish the defendants' liability for fraudulently creating an illusion of profitability and a false sense of security when the undisclosed facts suggest otherwise. The fact that the Planco marketing brochures may have varied slightly from broker to broker and customer to customer is not controlling here. Plaintiffs allege not that the promotional materials themselves were uniform, but rather that the information they contained—and hence that the broker-dealers disseminated—was uniformly misleading. Thus, at the very outset, the common issue of fact uniting all SPDA purchasers is

whether the Planco sales literature to which they were exposed was distorted by identical half-truths and omissions that materially affected their investment decisions. Following closely are common questions of the broker-dealers' own culpability in utilizing these materials and in failing to detect and disclose information that would have revealed the SPDAs' shaky foundations. Liability in this case does not depend on proof of the individual, face-to-face dealings between the class members and the registered representatives of the broker-dealers, and slight differences in the class members' positions will not defeat their common status as alleged victims of similar misrepresentations. *See Blackie* v. *Barrack*, 524 F.2d 801, 902 (9th Cir. 1975), *cert. denied*, 429 U.S. 816 (1976). The wrongful conduct alleged by plaintiffs occurred at the management level, if it did, and manifested itself in the defendants' course of promoting and selling the SPDAs. As a result, the relevant questions are readily susceptible to class-wide proof.

Indeed, inquiries into the actual sales process are of secondary importance. Plaintiffs are not required to establish how each and every SPDA was sold in order to prove that the SPDAs were securities. Similarly, it is not fatal to class certification that a particular investor did not receive or rely upon the contents of a Planco brochure. In a case such as this where liability would rest primarily on a failure to disclose material facts, positive proof of reliance is not a prerequisite to recovery. *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128, 153-54 (1972). Similarly, the presence of oral representations or embellishments proffered by an account representative will not rend this class, even if they were the sole basis for an individual's decision to purchase an SPDA. Unlike *In Re Scientific Control Corp. Securities Ltd.*, 71 F.R.D. 491 (S.D.N.Y. 1979), and other cases where claims based on oral representations were denied class status, in this case the representations related to objective factors—the issuer's financial stability or the safety, yield and liquidity of the SPDAs—that originated from a common source: the Planco documents or the broker-dealers' alleged refusal to conduct their own investigations. *See Korn* v. *Franchard Corporation*, 456 F.2d 1206, 1212 (2d Cir. 1972). Even proof of a material variance

among the representations will not defeat the class if certain omissions, inferred from their absence in the Planco literature, were common to all. *See Esplin* v. *Hirschi*, 402 F.2d 94, 99-100 (10th Cir. 1968), *cert. denied*, 394 U.S. 928 (1969).

The defendants also argue that individual questions relating to the timeliness of certain securities claims predominate over any common issues that may exist. The Court disagrees. Camouflaged as an attack on commonality, this argument in fact invites the Court to examine and accept in the course of these class certification motions an affirmative defense that is potentially dispositive of several claims in this litigation. Such inquiry is outside the scope of Rule 23 and indeed defies the principle enunciated in *Eisen* v. *Carlisle & Jacquelin*, 417 U.S. 156 (1974), that a court may not review the substantive issues raised in a class complaint when determining the claims' suitability for class treatment. *See, e.g., Chevalier* v. *Baird Savings Association*, 72 F.R.D. 140, 150 (E.D. Pa. 1976); *see also Mersay* v. *First Republic Corporation of America*, 43 F.R.D. 465, 471 (S.D.N.Y. 1968) (class certified notwithstanding individual questions as to statute of limitations).

Accordingly, the Court concludes that common issues of fact predominate in these actions and that the requirements of Rule 23(a)(2) have been satisfied.

Typicality

The third prerequisite for maintaining a class action under Rule 23 is that the individual claims advanced by the named plaintiffs are sufficiently typical of those asserted by the class members they purport to represent. Rule 23(a)(3), F.R.Civ.P. As a general rule, a plaintiff's claim meets the typicality requirement if it arises from the same events or course of conduct that gives rise to the claims of other class members and if it is based on evidence and legal theories consistent with the other members' claims. *Dura-Bilt Corporation* v. *Chase Manhattan Corp.*, 89 F.R.D. 87, 99 (S.D.N.Y. 1981). The test, ultimately, is whether the class representative will promote the interests of the class as he protects his own.

Because this inquiry focuses on the nature of the claims asserted, factual differences involving the date, type and manner of the purchase, the investor's perception of the transaction, or even the information furnished to him at the time will not destroy typicality if each class member was the victim of the same material omissions and the same consistent course of conduct. *See Dura-Bilt, supra; Oscar Gruss & Son* v. *Geon Industries, Inc.*, 75 F.R.D. 531, 534-35 (S.D.N.Y. 1977). This is so even though, as the defendants claim, the amount and type of information available to the public changed constantly throughout the class period, and the named plaintiffs supposedly had purchased their SPDAs at a time when Baldwin-United enjoyed good financial health. The lynchpin of plaintiffs' claim is the alleged nondisclosure of material facts relating to Baldwin-United's solvency; whether the named plaintiffs can prove an actionable omission to sustain their claims invites comment on the merits, which is forbidden in the context of this class certification motion. *See Eisen,* 417 U.S. at 178. Moreover, this Court finds that the putative class representatives will have a strong incentive to develop evidence pertaining to the entire class period because their claims rely on proof of a consistent course of conduct that extended beyond the instances of alleged fraud unique to them.

Similarly, the presence of common law issues in these complaints does not destroy typicality, even though the named plaintiffs will be called upon to represent individuals of many different states if a class is certified. Common law fraud substantially includes the 10b-5 claims, and the Court can order separate hearings to resolve the question of damages, if the need arises.

Notwithstanding certain variations in proof among members of the prospective class, the Court finds that the plaintiffs have satisfied the typicality requirement by showing that the same allegedly unlawful conduct affected all members of the prospective class.

Adequacy of Representation

Finally, before certifying the named plaintiffs as class representatives, the Court must be convinced that they will fairly and adequately protect the interests of the absent class members. Rule 23(a)(4), F.R.Civ.P. Although it is not necessary that the putative representatives' claims are identical to those of the class, the constraints of due process preclude class certification if the named plaintiffs possess other, potentially conflicting interests that would impair the vigorous prosecution of the class claims. *See Hansberry* v. *Lee*, 311 U.S. 32 (1940). As set forth above, factual differences involving the sales transaction, for example, the type of promotional material used by the various account representatives and the extent to which the purchaser relied on it, will not defeat class certification. Similarly unpersuasive is the argument, also proffered above, that the plaintiffs who purchased their SPDAs early in the class period have no incentive to prove facts relevant to a purported fraud committed on a subsequent purchaser. Nor can there by any question as to the qualifications, industry and commitment of plaintiffs' counsel. All class members stand or fall on the issue whether material information was misrepresented or withheld from SPDA purchasers, and the Court believes that the named plaintiffs will pursue this issue vigorously.

The Court therefore concludes that each of the prerequisites of Rule 23(a) is satisfied. In addition, the Court finds pursuant to Rule 23(b)(3) that questions of law and fact common to the members of the class predominate over any questions affecting only individual members, and that a class action is the superior method of adjudicating this controversy fairly and adequately.

Shearson Lehman argues that arbitration, which is available upon request to each putative class plaintiff in the Shearson Lehman track of cases, is a less expensive, more efficient—and hence superior—alternative to class litigation on certain arbitrable securities claims. Even assuming for the argument that our Court of Appeals' decision in *McMahon* v. *Shearson/American Express, Inc.*, 788 F.2d 94, 96 (2d Cir. 1986), was

wrong, *cf. Dean Witter Reynolds, Inc.* v. *Byrd*, ____ U.S. ____, 105 S.Ct. 1238, 1240 n. 1 (1985), and that Shearson Lehman enjoys, as it claims, an absolute right to compel arbitration pursuant to sales agreements it entered into with its SPDA customers, this Court does not agree that class treatment is perforce inappropriate as to those claims. The fairness and completeness of class litigation, in contrast to the scattered and fairly random solution suggested by individual arbitration, persuades this Court that fraud claims such as these are often best resolved by class action. Not only are interests of consistency, efficiency and completeness served, but there is also the assurance that most if not all potential claimants will be apprised of their rights and of the named plaintiffs' comparatively inexpensive efforts to vindicate them. This Court finds it hard to believe that any class action defendant so situated would prefer separate arbitration of each of thousands of potential claims that might otherwise be decided by class action at far less transactional cost. At least under the circumstances of this case, arbitration cannot be regarded as a serious alternative to the class action, which is so ideally suited to securities fraud claims.

The standards of Rule 23, at once fair and flexible, reaffirm the known truth that for all its pretensions, law is meant to be practical. The willingness of tweny-four sophisticated broker-dealers, advised by experienced counsel, to settle their companion actions for a record $183 million eloquently bespeaks the appropriateness of class certification among those actions that remain.

Accordingly, plaintiffs' motions for class certification in each of the four litigation tracts is granted. Each class shall be composed of those persons and entities (a) who purchased SPDAs (i) that were issued by National Investors Life Insurance Company and University Life Insurance Company of America and/or reinsured by National Investors Pension Insurance Company, Mt. Hood Pension Insurance Company, National Equity Life Insurance Company, and S & H Life Insurance Company, all of which are affiliated with Baldwin-United Corporation, and (ii) that were purchased through the respective broker-dealer defendants in each such action during

the period January 1, 1979 through July 13, 1983, each in his, her or its individual capacity and any and all collective representatives, assigns, heirs, executors, administrators, custodians, predecessors or successors in interest and any other person having any legal or beneficial interest in any of such SPDAs, and (b) who continued to hold such SPDAs on July 13, 1983.

The respective representatives of the Class as to each of the above-captioned actions shall be and hereby are certified to be as follows:

1. *Linton* v. *Shearson Lehman/American Express, Inc., et al.*, 83 Civ. 8476 (CLB), Alfred Linton and Jerome W. Eichelsbacher;

2. *Erti* v. *Paine Webber Jackson & Curtis, Inc., et al.*, 83 Civ. 9085 (CLB), Vincent Erti, Joseph and Elizabeth Chupko, George and Margaret Ledney, William Neil Aicholtz and Janet Aicholtz, and Genevieve Novicky;

3. *Woods* v. *W.H. Newbold's Sons & Co., Inc., et al.*, 84 Civ. 2235 (CLB), Oscar J. Woods; and

4. *Perel* v. *Rotan Mosle, Inc.*, 84 Civ. 8879, Steven A. Perel.

Settle a formal order on notice, which shall declare the classes as hereinbefore set forth and provide for notice and an opportunity to the members of the classes to exclude themselves.

Dated: White Plains, New York
June 27, 1986

/s/ CHARLES L. BRIEANT

Charles L. Brieant
U. S. D. J.